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In The Supreme Court of the United States

McLANE WESTERN, INC.,

Petitioner,

v.

DEPARTMENT OF REVENUE, STATE OF COLORADO, ET AL.,

Respondents.

On Petition For A Writ Of Certiorari To The Colorado Court Of Appeals Division IV

BRIEF OF *AMICUS CURIAE* INSTITUTE FOR PROFESSIONALS IN TAXATION IN SUPPORT OF PETITIONER

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BRIEF OF INSTITUTE FOR PROFESSIONALS IN TAXATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER[1]

This brief is submitted by the Institute for Professionals in Taxation (the "Institute") as *amicus curiae* in support of the Petition for a Writ of Certiorari filed by Petitioner, McLane Western, Inc., dated April 7, 2006, seeking review of the Colorado Court of Appeals' opinion in *McLane Western, Inc. v. Department of Revenue*, 126 P.3d 211 (Colo.Ct.App. 2005), *cert. denied*, 2006 WL 349738 (Colo. Jan. 9, 2006).

I. STATEMENT OF INTEREST OF *AMICUS CURIAE*

The Institute for Professionals in Taxation (or as it is sometimes known, IPT) is an Internal Revenue Code § 501(c)(3) non-profit educational association with members representing corporations, firms, or taxpayers throughout the United States and Canada. It educates, certifies and establishes strict codes of conduct for property, income, and sales and use tax professionals who represent taxpayers. The Institute provides educational opportunities for its members tailored to their professional needs. Professional designation programs in property, income and sales tax leading to the CMI designation

[1] Petitioner, McLane Western, Inc., and Respondent, Colorado Department of Revenue, have consented to the filing of this brief, and their letters of consent have been filed with the Clerk of the Court.

No counsel for a party authored this brief in whole or in part, and no person or entity other than *amicus curiae*, its members, or counsel has made a monetary contribution to the preparation or submission of this brief.

(Certified Member of the Institute) are available to members who satisfy the educational, experience and examination requirements. The Institute is dedicated to the uniform and equitable administration of ad valorem, income and sales and use taxes, to minimizing the cost of tax administration and compliance, and to a high degree of professionalism. Members are expected to adhere to a strict Code of Ethics and Standards of Professional Conduct. IPT members represent the spectrum of business and industry sectors of all sizes – from small firms to Fortune 500 companies, and they share a dedication to further professionalism and cooperation within the tax profession. The Institute and its members therefore have a vital and direct financial interest in prohibiting discriminatory state taxes and in a principled construction of the Commerce Clause.

II. SUMMARY OF ARGUMENT

The imposition of the Colorado tobacco excise tax results in a tax being levied on different tax bases, thereby causing some vendors to pay a higher tax on the same product, to the benefit of Colorado distributors and manufacturers, and to the detriment of out-of-state competitors. The Court should grant certiorari to consider whether the Colorado excise tax, and any other like it that may be enacted throughout the country, contravenes years of Commerce Clause jurisprudence.

III. ARGUMENT

The constitutional analysis adopted by the Colorado Court of Appeals in upholding the Colorado tobacco excise tax as applied to Petitioner, McLane Western, Inc., is

incorrect and inconsistent with the Court's prior interpretation of the Commerce Clause. The Colorado Court of Appeals impermissibly permits the excise tax to be imposed on a different ("shifting") tax base, where that tax base differs depending on whether the distributor or seller of tobacco products is located in Colorado or outside the state.

The decision below creates a competitive disadvantage in the marketplace that is contrary to the Commerce Clause doctrine barring discrimination against products and activities crossing state lines. The Colorado Court of Appeals incorrectly interpreted the Court's Commerce Clause cases by limiting the impact of the Commerce Clause to tax statutes that involve either a difference in tax rates or an exemption from taxation, while permitting a statute that imposes taxes on different tax bases.

If the decision below is allowed to stand, it will provide a broad loophole for states to discriminate against interstate commerce and to evade constitutional challenge by the mere expedient of changing the wording in the state tax statute to eliminate differential tax rates or exemptions. The Colorado Court of Appeals' interpretation of the Court's prior cases is incorrect and results in improper and unconstitutional tax policy that warrants the Court's review.

A. The Colorado Court of Appeals Decision Upholding the Colorado Tobacco Excise Tax Violates the Commerce Clause Because The Colorado Statute Imposes a Different Tax Base on Taxpayers When the Economic Activity Occurs Outside Colorado.

Petitioner McLane Western, Inc. buys tobacco products other than cigarettes, also known as Other Tobacco

Products ("OTP"), from United States Smokeless Tobacco Products, Inc. ("Sales"). Petitioner is located in Colorado. Sales in turn purchases the OTP from United States Smokeless Tobacco Manufacturing, L.P. ("Manufacturing"). Both Sales and Manufacturing are located outside Colorado. Colorado imposes an excise tax on OTP distributed in the state. Colo. Rev. Stat. § 39-28.5-102(1). *See* Petition, App. E at p. 28a. The OTP excise tax of 20% is imposed by Colorado on the first Colorado distributor (essentially upon receipt of the product by that distributor, which here is the invoice price paid by Petitioner to Sales). Because the sales price charged in each segment of the distribution claim is increased ("marked up") to reflect additional marketing costs and profits incurred by the out-of-state companies, the ultimate purchase price paid by Petitioner to Sales for OTP products sold in Colorado is a higher price than if the same products were purchased from a Colorado-based distributor. 126 P.3d at 214.

The disparate economic impact of the Colorado statute can be summarized as follows: when the manufacturer, distributor and seller are located outside Colorado, the tax base and resulting tax burden created by the Colorado statute will be higher than where even one of those entities is located in Colorado. In the instance where the entities are located in Colorado, the excise tax is imposed on the lower price paid by the first Colorado distributor before the price has been marked up.

The imposition of the Colorado OTP excise tax on Petitioner's purchase of OTP violates the third prong of the *Complete Auto Transit* test because it unduly burdens interstate commerce, is discriminatory, and is in violation of the Commerce Clause. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). The Colorado OTP excise tax

imposes a greater tax burden on Colorado sellers who purchase from out-of-state distributors than those who purchase from in-state distributors.

The Colorado Court of Appeals acknowledged this difference in the tax base and tax burden, before erroneously concluding that because the Colorado tax statute reflects a mere difference in the tax base (what it called the "shifting tax base"), the Colorado tax statute is not facially discriminatory, nor does the statute discriminate against out-of-state competitors in violation of the Commerce Clause. 126 P.3d at 216. The Colorado Court of Appeals determined that cases interpreting the Commerce Clause require there to be a difference in either tax rates or exemptions before there can be any discriminatory impact. 126 P.3d at 214. But the Commerce Clause cases on which it relied do not support that conclusion. The Commerce Clause instead clearly prohibits a state statute like the Colorado OTP excise tax that requires a higher and discriminatory tax base to be imposed on products produced in part, or distributed in part, outside the State. The Court should grant certiorari to consider whether a state tax statute violates the Commerce Clause regardless of whether the discrimination factor is found in the tax rate, in exemptions from the tax, or in the tax base on which the tax is calculated.

The Colorado OTP excise tax violates the Commerce Clause for the same reasons set forth in *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963), where the Court held that a Louisiana sales tax imposed on oil drilling equipment is unconstitutional where it included a different and discriminatory tax base for equipment purchased from another state. The Louisiana statute did not employ a different tax rate or tax exemption, but

employed a discriminatory tax base that had the same economic result as the Colorado OTP excise tax does here. The Court stated in *Halliburton*, 373 U.S. at 70:

> The inequality of the Louisiana tax burden between in-state and out-of-state manufacturer-users is admitted. Although the rate is the same, the appellant's tax base is increased though the inclusion of its product's labor and shop overhead.

The discriminatory effect of the Colorado OTP excise tax parallels that caused by the state regulation recently criticized by the Court in *Granholm v. Heald*, 544 U.S. 460 (2005). In striking down a state regulatory system that imposed greater restraints on out-of-state than in-state wine distributors, the Court stated unequivocally that "in all but the narrowest circumstances, state laws violate the Commerce Clause if they mandate differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." 544 U.S. at 472 (quoting *Oregon Waste Sys., Inc. v. Department of Environmental Quality*, 511 U.S. 93, 99 (1994)).

The Court similarly recognized in *Granholm* that the proscribed discrimination arises whenever certain vendors are required by the tax system to pay higher fees, costs or taxes, or are subjected to greater licensing or regulatory requirements, 544 U.S. at 474:

> The differential treatment requires all out-of-state wine [distributors], but not all in-state wine [distributors], to pass through an in-state wholesaler and retailer before reaching consumers. These two extra layers of overhead increase the cost of out-of-state wines to Michigan consumers.

The Court has consistently ruled that taxes must be imposed on in-state and out-of-state taxpayers in a non-discriminatory and substantially equivalent manner. As it stated in *Associated Industries of Missouri v. Lohman*, 511 U.S. 641 (1994):

> To ensure that the State is indeed merely imposing countervailing burdens on comparable transactions, we have required that the taxes on interstate and intrastate commerce be imposed on "substantially equivalent event[s]."

Id. at 647 (quoting *Maryland v. Louisiana*, 451 U.S. 725, 759 (1981)).

The Court should grant certiorari to consider whether the Colorado Court of Appeals properly applied this precedent when it held, 126 P.3d at 216:

> The fact that the tax base calculated on the price paid by the taxable distributor may place the product at a competitive disadvantage in the market place because the higher tax is added to the price does not, in our view, render the tax unconstitutional under the Commerce Clause.

Although the Court of Appeals acknowledged the competitive disadvantage placed on distributors purchasing products from out of state, its decision ignores the practical operation of the Colorado OTP excise tax, which unquestionably favors a distributor purchasing from within Colorado over a distributor purchasing from outside Colorado. The Court has repeatedly stressed that under the Commerce Clause a state may not discriminate, no matter what form the discrimination takes, and no matter the mechanics of the statutory scheme that produce the discrimination. The Court has instead flatly

stated that "actual discrimination, wherever it is found, is impermissible." *Associated Industries of Missouri*, 511 U.S. at 650.

The Court emphasized the fundamental fact that the Commerce Clause forbids discrimination, regardless of the form it takes, in *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186 (1994):

> Our Commerce Clause jurisprudence is not so rigid as to be controlled by the form by which a State erects barriers to commerce. Rather our cases have eschewed formalism for a sensitive, case by case analysis of purposes and effects. As the Court declared over 50 years ago: "The Commerce Clause forbids discrimination, whether forthright or ingenious. In each case it is our duty to determine whether the statute under attack, whatever its name may be, will in its practical operation work discrimination against interstate commerce."

Id. at 201 (quoting *Best & Co. v. Maxwell*, 311 U.S. 454, 455-456 (1940)).

The plain fact that a taxpayer purchasing from an out-of-state supplier pays a higher tax has a direct effect on the taxpayer's sales price and profit margin. This tax effect clearly gives the taxpayer who purchases products from in-state suppliers the ability to charge a lower price or increase its profit margin. The Court has repeatedly held that this type of competitive advantage is contrary to the fundamental principles of the Commerce Clause and the Court's own decisions. *See Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 329 (1977) ("No state, consistent with the Commerce Clause, 'may impose a tax which discriminates against interstate commerce . . . by

providing a direct commercial advantage to local business.'" (quoting *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 457 (1959)).

Whether intentional or unintentional, Colorado has created a clear preference for purchasers of in-state products. The Court has stressed that "[T]he prohibition against discriminatory treatment of interstate commerce follows inexorably from the basic purpose of the Clause. Permitting the individual States to enact laws that favor local enterprises at the expense of out-of-state business would invite a multiplication of preferential trade areas destructive of the free trade which the Clause protects." *Boston Stock Exchange*, 429 U.S. at 329. The purchaser of out-of-state products cannot operate on a fair playing field if it is paying a higher *tax*, even though the tax *rate* may be the same. Certiorari should therefore be granted.

B. The Colorado Court of Appeals Decision Upholding the Colorado Tobacco Excise Tax Would Allow Other States to Impose Discriminatory Taxes on Taxpayers When the Economic Activity Takes Place Outside the Taxing State.

The Court of Appeals' decision, if allowed to stand in its present form, would enable a state to draft or redraft a tax statute to withstand constitutional challenge merely by changing its wording to eliminate differential tax rates or exemptions, even while purposely discriminating between taxpayers based solely on the applicable tax base. Not only would this contravene *Halliburton*, and permit states to do an end run around existing Commerce Clause jurisprudence, but it would be poor tax policy.

The decision below threatens to resurrect the very sort of tax statute expressly struck down by the Court in *Armco, Inc. v. Hardesty*, 467 U.S. 638 (1984). The West Virginia gross receipts tax struck down in *Armco* imposed a tax on wholesale operations, but exempted in-state manufacturers. Under the Colorado Court of Appeals' reasoning, however, similar statutes could now be enacted to eliminate the tax exemption for in-state manufacturers, instead imposing it on both wholesaling and manufacturing and making it applicable to the first taxable event in the state. The economic result would be similar to the result in Colorado – it would permit what the Colorado Court of Appeals called the "shifting tax base" and thereby discriminate against out-of-state manufacturers and distributors. The same result condemned in *Haliburton* would become constitutionally permissible, at least in the view of the Colorado appellate court. The Court should grant certiorari to address this anomalous result.

IV. CONCLUSION

The Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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